In case of discrepancies between the French and the English text, the French text shall prevail

Luxembourg, 21 January 1991

To all Luxembourg undertakings for collective investment and to all those that take part in the functioning and control of these undertakings

Circular IML 91/75

as amended by Circulars CSSF 05/177 and CSSF 18/697

Re: **Revision and remodelling of the rules to which Luxembourg undertakings governed by the Law of 30 March 1988 on undertakings for collective investment ("UCI") are subject.**

Ladies and Gentlemen,

This circular repeals and replaces IML Circular 88/48 of 8 April 1988 as well as the previous circulars which remained applicable to UCIs following the entry into force of the aforementioned Law of 30 March 1988.

The circulars thus repealed, in addition to IML Circular 88/48 of 8 April 1988, are circulars VM/47 of 7 August 1978, VEF/48 of 7 November 1978, IML 84/12 of 8 March 1984, IML 84/13 of 9 March 1984, IML 84/15 of 30 March 1984, IML 85/23 of 25 March 1985 and IML 88/47 of 5 April 1988.

In accordance with its objective of clarification and simplification, the main purpose of this circular is to adapt and to clarify the rules of the repealed circulars in light of the experience acquired during the practical application thereof and to reproduce the rules thus revised in one single text according to the following summary:

SUMMARY

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Chapter A. Purpose and scope of the Law of 30 March 1988.

The purpose of the Law of 30 March 1988 is the protection of the investor who is solicited by promoters whose activity is the raising of funds in order to invest them collectively in accordance with the principle of risk-spreading.

In accordance with its objective, the Law of 30 March 1988 determines the legal and regulatory frame in which this activity may be exercised and pursuant to which it is submitted to the supervision of the *Institut Monétaire Luxembourgeois* ("IML") which is the supervisory authority.

The exercise of the activity subject to the Law of 30 March 1988 is exclusively restricted to those undertakings which qualify as UCIs in accordance with the definition given in Chapter B. hereafter; it therefore follows that such an activity, if exercised in Luxembourg, must be considered as illegal where it is exercised outside the scope of this Law.

On the other hand, an undertaking which in practice, does not meet all conditions for application of the Law of 30 March 1988 may not claim the status of a UCI by voluntarily submitting to the provisions of the Law.

Chapter B. Definition of the meaning of UCI.

I. Criteria by which the meaning of UCI is being defined.

In order to qualify as an activity governed by the Law of 30 March 1988, it is required, and it suffices, that the following conditions are cumulatively met:
- the collective investment of savings;
- the savings used for collective investment must have been collected from the public;
- the investment which forms the object of the collective investment must be made in accordance with the principle of risk-spreading.

Collective investment of savings shall be taken to mean the collective investment of funds collected individually from the public. This investment may be made in transferable securities or other assets. The objective is to obtain a yield or a capital gain. Hence the objective of UCIs is not to acquire an interest for a purpose beyond that of obtaining a yield, namely to secure influence or even control. Furthermore, the holding of such an interest entails a long-term holding objective, whereas for UCIs the retention of assets in the portfolio only depends upon the yield or the capital gains potential thereof. By way of exception, certain types of UCIs, such as those investing in venture capital, may sometimes acquire more substantial interests in companies of which they hold shares and even intervene in the management of such companies by the appointment of one or several representatives to the board of directors. Such involvement, however, does not have control as an objective but is dictated by the particular nature of the investments of such undertakings.

The public is solicited when the collection of funds, with the objective of collective investment, is not restricted to a small circle of persons only.
With respect to the principle of risk-spreading, the purpose of its application is to prevent an excessive concentration of the investments in the context of the collective investment.

The aforementioned definition criteria are common to all categories of UCIs provided for by the Law of 30 March 1988. Indeed, depending upon the category to which they belong, UCIs governed by the Law of 30 March 1988 only differ from one another by their legal form or by their collective investment objective.

II. Practical application of the criteria retained for the definition of the meaning of UCI.

In principle there is no problem to determine whether the conditions for application of the Law of 30 March 1988 are met in the cases of common funds ("FCP") and investment companies with variable capital ("SICAV"). In the case of undertakings which do not have the legal form of common fund or SICAV, it is however sometimes difficult in practice to determine whether the Law of 30 March 1988 is applicable to them or not. In such cases, the supervisory authority will in the first instance rely on the definition criteria set out in the preceding Section I. in order to determine whether such undertakings do or do not meet the required conditions for UCI qualification.

If the review of the application file based on these criteria is not sufficient to conclude with the necessary certainty as to whether the Law of 30 March 1988 is applicable, further elements will have to be taken into account such as the organisation and the general structure of such undertakings, i.e. the systematic redemption of shares, the existence of an investment advisory company, the charging of commissions both on the purchase of securities in such undertakings and for the management thereof.

Thus, in application of the preceding principles, financial investment companies set up with the purpose of control, are excluded from the scope of application of the Law of 30 March 1988 because their activity is not the collective investment of savings. The same applies to family holding companies and investment clubs which, even though their objective is the collective investment of savings, do not collect savings from the public.

Chapter C. Classification of UCIs situated in Luxembourg.

A UCI shall be deemed to be situated in Luxembourg if the registered office of the management company of the common fund or the registered office of the investment company is situated in Luxembourg. UCIs situated in Luxembourg will be referred to hereafter as Luxembourg UCIs.

Depending on their characteristics, Luxembourg UCIs will be subject to Part I or Part II of the Law of 30 March 1988.

This classification makes it possible to distinguish between
- undertakings within the meaning of Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (the "85/611/EEC Directive"); and
- the other undertakings which do not fall within the scope of application of the 85/611/EEC Directive.

The consequences of this distinction are described in more detail in section III. hereafter.

I. Definition of UCIs governed by Part I of the Law of 30 March 1988.

Part I of the Law of 30 March 1988 applies to all undertakings for collective investment in transferable securities ("UCITS") which are defined as being UCIs the exclusive object of which is the investment in transferable securities.

Considering this definition, the criterion which determines whether a UCI is subject to Part I or Part II of the Law of 30 March 1988 is the intended investment objective. If the undertaking invests in transferable securities, it is subject to Part I, apart from the exceptions referred to in Section II. hereafter.

UCITS subject to Part I of the Law of 30 March 1988 are of the open-ended type, since the rules to which they are subject provide for the obligation to directly or indirectly redeem their units or shares at the request of the investors.

II. Definition of UCIs governed by Part II of the Law of 30 March 1988.

Part II of the Law of 30 March 1988 applies to all UCIs the principal object of which is the investment in securities other than transferable securities and to all UCITS excluded from Part I.

In its Article 2, the Law of 30 March 1988 provides for exceptions to the basic rule reproduced in Section I. above, by excluding from the scope of application of Part I certain categories of UCITS. This is the transposition in national law of the corresponding provisions of the 85/611/EEC Directive.

The following types of UCITS are concerned by this exclusion:

1. UCITS of the closed-ended type. These UCITS can be defined by distinguishing them from open-ended UCITS which directly or indirectly redeem their units or shares at the request of investors.

   The reimbursement to investors after a decision of the management bodies is not tantamount to a redemption if such reimbursement occurred without any request from investors where such a request would have been based on a right to request redemption.

   If the securities issued by UCITS of the closed-ended type are redeemed at the request of investors after a certain date, such an undertaking shall fall within the scope of application of Part I of the Law of 30 March 1988 from such date onwards, unless it belongs to one of the other categories of UCITS described in paragraph 2. to 4. hereafter. In case this feature is established at inception, the prospectus must from the outset draw the investors' attention to that fact and to the eventual consequences thereof, particularly on the investment policy.

A UCITS, the constitutional documents of which provide for the right of investors to request redemptions, cannot qualify as being of the closed-ended type and as such falls outside the scope of application of Part I of the Law of 30 March 1988, upon the grounds that it provides for limitations on the exercise of such a right. As a UCITS subject to the provisions of Part I, it must relinquish such limitations insofar as their purpose is to subject the exercise of the right to redeem to conditions and procedures which render redemptions practically impossible or unnecessarily and arbitrarily complicated or provide for unnecessary and arbitrary intervals.

2. UCITS which raise capital without promoting the sale of their units or shares to the public within the European Economic Community ("EEC") or any part of it.

The exclusion from Part I of the Law of 30 March 1988 does not dispense the UCITS concerned from the condition of the collection of public savings which all undertakings must comply with in order to qualify as a UCI; it simply prohibits the UCITS in question to engage in any promotional activity within the EEC; the term "promotional activity" refers in particular to the use of advertisement methods such as press, radio, television or advertisement circulars. It does not however refer to offers for subscription which are addressed to a limited, particularly knowledgeable circle of investors such as pension funds and insurance companies.

It follows from the above that the UCITS concerned hereby are those which, even though they are addressed to the public, refrain from performing any promotional activity within the EEC.

3. UCITS whose units or shares, as restricted by their constitutional documents, may only be sold to the public in countries which are not members of the EEC.

UCITS whose units or shares are listed on the Luxembourg Stock Exchange and whose units or shares are marketed solely outside the EEC fall into this category.

The supervisory authority does not intervene in the delimitation of the scope of application. The exclusion only operates subject to the condition that the management regulations or the articles of incorporation of these UCITS provide expressly that the sale of their units or shares is limited to the public of countries which are not members of the EEC.

4. Categories of UCITS determined by the supervisory authority for which the rules laid down in Chapter 5 of the Law of 30 March 1988 are inappropriate in view of their investment and borrowing policies.

UCITS covered by this exclusion belong to one of the following categories:

4.1. Undertakings the investment policy of which provides for the investment of 20% or more of their net assets in venture capital. Investment in venture capital shall be taken to mean investment in securities of companies which have been recently constituted or which are still in the early development stage.

4.2. Undertakings the investment policy of which provides for the investment of 20% or more of their net assets (other than liquid assets) in securities other than the transferable securities provided for in Article 40(1) of the Law of 30 March 1988.

4.3. Undertakings the investment policy of which provides for the permanent borrowing for investment purposes of at least 25% of their net assets.

4.4. Undertakings the investment policy of which provides for the investment of 20% or more of their net assets in other open-ended UCIs.

4.5. Undertakings the investment policy of which provides for the investment of 20% or more of their net assets in money market instruments and liquid assets (including any regularly negotiated money market instruments the residual maturity of which does not exceed 12 months) other than the transferable securities provided for in Article 40(1) of the Law of 30 March 1988.

4.6. Undertakings the investment policy of which provides for the investment of 50% or more of their net assets in liquid assets.

4.7. Multiple compartment undertakings, one compartment of which is not subject to Part I of the Law of 30 March 1988 by reason of its investment or borrowing policy.

III. Status of UCITS (Part I) and other UCIs (Part II) in the European context.

For the regulation of UCITS subject to it, Part I of the Law of 30 March 1988 takes as a basis the provisions of the 85/611/EEC Directive. Consequently, these UCITS conform to the entirety of the requirements of those provisions. They thus benefit from the status of EEC UCITS which gives them the right to freely market their units or shares in the whole of the territory of the EEC.

UCIs, other than UCITS governed by Part I of the Law of 30 March 1988, may not rely upon the marketing facilities provided for by the 85/611/EEC Directive since they are excluded from the scope of application thereof. Consequently, where such UCIs wish to market their units or shares in other countries of the EEC, they must comply with the specific conditions to which the authorities of the countries concerned may, as the case may be, subject the authorisation of UCIs which do not have the status of EEC UCITS.

Chapter D. Rules concerning the central administration of Luxembourg UCIs.

Under the provisions of the Law of 30 March 1988, the central administration of all Luxembourg UCIs must be situated in Luxembourg. This requirement ensures that the supervisory authority, the depositary and the *réviseur d'entreprises* (statutory auditor) may easily perform their respective legal duties.

I. Definition of the meaning of central administration in Luxembourg.

The legal requirement that central administration be situated in Luxembourg implies *inter alia* that:

- the accounts must be compiled, and the accounting documents must be available, in Luxembourg;
- issues and redemptions must be carried out in Luxembourg;
- the register of unitholders must be kept in Luxembourg;
- the prospectus, financial reports and all other documents intended for investors must be established in cooperation with the central administration in Luxembourg;
- the correspondence, dispatch of financial reports and of all other documents intended for shareholders or unitholders must be carried out from Luxembourg and in all cases under the responsibility of the central administration in Luxembourg;
- the calculation of the net asset value must be carried out in Luxembourg.

It appears from the preceding list that the meaning of central administration in Luxembourg exclusively comprises accounting and administrative functions. It therefore neither excludes the possibility for Luxembourg UCIs to obtain assistance for the management of their assets from investment advisers established abroad nor does it prevent that the decisions in relation with that management (investment and disinvestment decisions) are made and executed elsewhere than in Luxembourg.

II. Organisation of the central administration in Luxembourg.

A Luxembourg UCI or its management company, where it takes the form of a common fund, is not obliged to perform itself the tasks relating to the accounting and administrative duties of the central administration in Luxembourg.

By means of a service contract, it may indeed entrust the exercise of those duties which essentially concern the execution of the tasks set out in section I. above to a third party established in Luxembourg. Upon the condition that a division of such tasks is not detrimental to the satisfactory performance of the central administration, this third party may delegate the execution of specific tasks to one or more other providers of services established in Luxembourg subject to it ensuring the coordination, general supervision and liability therefor.

It is also conceivable that a Luxembourg UCI may, by means of separate service agreements, organise itself the division of tasks connected to the duties of central administration amongst various providers of services established in Luxembourg provided that in such cases, it is in a position to coordinate and supervise itself the execution of such tasks unless it entrusts such a mission to a duly qualified third-party agent. Such a third-party agent then becomes the interlocutor of the IML in its relationship with the central administration of the relevant UCI.

In both cases, the division of tasks related to the duties of central administration must not result in an excessive fragmentation which renders the exercise of the coordination and general supervisory function difficult if not impossible or which unnecessarily increases costs by unjustified duplication.

For the reasons mentioned above, it is therefore recommended not to envisage constructions or structures that are too complicated or costly.

On the basis of the above, the IML considers that tasks as closely connected as the execution of issues and redemptions and the keeping of the register of unitholders may only be entrusted to one single provider of services. The IML considers furthermore that it is not conceivable to have different providers of services execute activities relating to the same task. Thus for instance, it is not admissible to have more than one provider of services perform the execution of the necessary tasks in relation with the keeping of the accounts.

In organising its relationship with the depositary of the UCI which it administers, the central administration in Luxembourg must, by the operation of appropriate procedures, ensure the proper functionning of information circuits and information flow necessary to obtain upon request from the depositary all information and data

required in order to determine the value of the assets and liabilities of the UCI and to calculate the net asset value.

The UCI, in the case where it ensures itself the administration, or the providers of services which may be appointed therefor, must have the necessary infrastructure in Luxembourg i.e. sufficient human and technical means in order to accomplish the entirety of the tasks connected to the duties of central administration in Luxembourg. This implies the locating in Luxembourg of equipment and material used by the central administration as technical support for the execution of its duties.

III. Execution of the accounting and administrative duties as defined by the notion of central administration in Luxembourg.

1. Keeping of the accounts, calculation of the net asset value and availability of core documentation relating to the UCI and its operations.

Where the central administration in Luxembourg uses a remote-access computing network as technical support for the execution of the tasks connected to the keeping of the accounts and/or the calculation of the net asset value (such as operations necessary for the valuation of the portfolio of securities, the determination of the amount of income generated by that portfolio and the conversion in the currency of account of the UCI of assets denominated in another currency), the requirement to locate in Luxembourg the equipment and material necessary for the operation of such an administration does not exclude that the unit which is intended to ensure the processing of accounting and other information which is entered in the network may be situated elsewhere than in Luxembourg.

An eventual location abroad of the processing unit is however subject to the following conditions:

- the central administration must have at its disposal in Luxembourg necessary means to enter information in the processing unit of the remote-access computing network used and to withdraw such information. Its access to the information recorded in the network processing unit must be immediate and unlimited and must *inter alia* permit the instantaneous and full production of any data necessary for normal operations;
- the central administration must be aware of the operating conditions of the processing unit and must give its consent for alterations to its programme;

- the central administration must have the possibility to directly intervene in the processing of information stored in the processing unit;
- information stored in the processing unit must be transferred upon each valuation of the assets, at least once a week and, as the case may be, more frequently, if required for security reasons, on servers which are situated and which may be operated in Luxembourg;
- the promoters must have at their disposal the necessary means to enable the central administration to continue to operate normally in case of exceptional events such as the interruption of the means of communication with the processing unit or the failure thereof for an extended period;
- where the central administration uses the remote-access computing network together with other users which are not involved in the operations of the UCI, the central administration must ensure by the establishment of adequate protection measures that these users may not, at the level of the processing unit, have access to the information concerning the UCI, in order to prevent them from obtaining knowledge of that information or altering or deleting it.

The conditions set out under the first, second, third and last indents above apply *mutatis mutandis* where the network processing unit used is situated in Luxembourg.

In principle, it is the central administration's responsibility to proceed from Luxembourg, as the case may be in cooperation with the depositary, with the operational process necessary to enter the information relating to the operations of the UCI into the remote-access computing network used irrespective of where the processing unit of the network is situated. This does not exclude that portfolio managers established abroad may immediately access the relevant network and set in motion the accounting operations connected to the execution of the decisions taken by them within the scope of their management mandate. Furthermore, it does not exclude that other agents involved in the operations of the UCI may proceed in the same way.

Such intervention by portfolio managers and by other agents whose services are being used, is however subject to the following conditions:
- the central administration must ensure by the establishment of adequate protection measures that these agents may not access information other than that which is necessary for the execution of their respective duties notwithstanding the provisions concerning professional secrecy;

- the UCI must install, at management level, supervisory procedures which are able to ensure the regularity of the operations initiated by the portfolio managers with respect to the obligations to which it is subject under the Law of 30 March 1988 as well as under its constitutional documents and prospectus.

Since the central administration in Luxembourg assumes the ultimate liability for the accuracy of the financial information relating to the UCI, it alone is authorised to proceed with the allocations, apportionments and provisions necessary for finalising the calculation of the net asset value, these operations concerning in particular the charges, expenses and taxes borne by the UCI.

The central administration must have at its disposal in Luxembourg all accounting and other documents which constitute the essential documentation of the UCI and which are necessary for:

- the preparation of accounts and valuations;
- the drawing-up of certificates of title and of debt securities;
- the determination of the allocation of units or shares outstanding and
- the general protection of the interests of the UCI such as the depositary agreement, the agreements made with the portfolio managers as well as any other agreements with providers of services involved in the operations of the UCI.

The requirement as to availability in Luxembourg of the essential documentation of the UCI implies that the documents relating to transactions initiated from abroad must immediately be forwarded to Luxembourg.

2. Execution of issues and redemptions.

2.1. Role of the central administration in Luxembourg in connection with the execution of issues and redemptions.

The requirement for issues and redemptions to take place in Luxembourg implies that the performance of the tasks related to the processing of subscription and redemption orders for the securities issued by Luxembourg UCIs, is to be carried out by the central administration in Luxembourg of such UCIs. This means that it is in principle the responsibility of the central administration in Luxembourg to determine the prices at which the subscription and redemption orders must be calculated, to draw up the subscription or redemption contract notes and the certificates of title and to dispatch such documents to the individual investors.

The requirement relating to the execution in Luxembourg of issues and redemptions does not prohibit Luxembourg UCIs from appointing Luxembourg or foreign intermediaries as authorised financial agents and representatives for the issue and redemption of their units or shares.

Such intermediaries are then authorised to collect subscription and redemption orders for the units or shares of the UCIs by which they have been appointed. Subject to the conditions specified under heading 2.2. hereafter, they may participate in the issue and redemption operations either as distributors, nominees or market makers.

It is understood that recourse to the intermediaries referred to above may in no way restrict the ability of investors to deal directly with the UCI of their choice when placing their subscription and redemption orders. It is therefore necessary for UCIs to explicitly and prominently mention this possibility in their prospectus.

2.2. Conditions to which intermediaries are subject before they may participate in issue and redemption operations.

2.2.1. Conditions applicable to distributors.

Distributors are intermediaries who are part of the distribution process set up by the promoters whether they actively participate in the marketing of the securities issued by a UCI or whether they are appointed in the prospectus or in any other document as being authorised to receive subscription and redemption orders on behalf of that UCI.

For the purposes of the processing of the subscription and redemption orders collected by them, the distributors must forthwith transmit to the central administration in Luxembourg the data necessary for the timely completion of the entirety of the tasks related to the processing of such orders.

Where the subscription or redemption orders concern registered securities, it is evident that distributors shall provide the central administration in Luxembourg with the registration data necessary to accomplish on an individual basis the tasks referred to above.

Subject to the provisions of heading 2.3. below, this obligation does not exist in case where the issue and redemption orders relate to bearer securities. In such cases, distributors act in the capacity of subscribers *vis-à-vis* the central administration in Luxembourg. They may therefore aggregate individual subscription and redemption orders and transmit them in the form of a combined order to the central administration in Luxembourg. In doing so, the distributors may, where appropriate after netting, purchase or sell the combined total of all securities subscribed to or redeemed from investors to be followed by the subsequent allocation thereof according to the individual orders received.

It is not necessary for distributors to forward to the central administration in Luxembourg the documentation relating to subscription and redemption orders from investors. However, where such documentation is not forwarded to Luxembourg, the distributors must allow the central administration in Luxembourg to have access thereto without any restriction, in case of need.

Where the distributors are authorised to receive and make settlement payments in respect of the subscription and redemption orders collected by them, they may aggregate and set off individual payments in order to deal on a net basis with the central administration in Luxembourg. This possibility is available for orders relating to registered shares and for orders relating to bearer shares.

In order to facilitate delivery of certificates, a Luxembourg UCI and its depositary may enter into an agreement with the distributors pursuant to which the latter are authorised to hold a stock of unissued certificates. In such cases, the distributors must be duly authorised by an agreement to deliver bearer certificates to subscribers in accordance with the instructions from the central administration in Luxembourg.

2.2.2. Conditions applicable to nominees.

Nominees act as intermediaries between investors and the UCIs of their choice.
Where the intervention of a nominee is an integral part of the distribution arrangement set up by the promoters, the relationship between the UCI, the nominee, the central administration in Luxembourg and the investors must be determined by contract which shall provide for their respective obligations. The promoters must nevertheless, ensure that the nominee presents sufficient guarantees for the proper execution of its obligations towards the investors who utilise its

services. The intervention of a nominee is only authorised if the following conditions are met:

a) the role of the nominee must be adequately described in the prospectuses;
b) the investors must have the possibility to directly invest in the UCIs of their choice without using a nominee and prospectuses must expressly state this fact;
c) the agreements between the nominee and the investors must include a termination clause which gives the investors the right to claim, at any time, direct title to the securities subscribed through the nominee.

It is understood that the conditions set out under items b) and c) are not applicable in circumstances where the use of the services of a nominee is indispensable or even compulsory for legal, regulatory or compelling practical reasons.

2.2.3. Conditions applicable to market makers.

Market makers are intermediaries which participate for their own account and at their own risk in subscription and redemption transactions on securities issued by UCIs.

Where the organisation of a market by such intermediaries is an integral part of the distribution arrangement set up by the promoters, the relationship between the UCI, the central administration in Luxembourg and the market makers must be determined by contract.

Additionally, the following conditions must be met:

a) the role of the market makers must be adequately described in the prospectuses;
b) the market makers may not act as counterparties to subscription and redemption transactions without the specific approval of the investors initiating the relevant transactions;
c) market makers may not price subscription and redemption orders addressed to them on less favourable terms than those that would be applied to such orders had they been directly processed by the relevant UCIs;
d) market makers must regularly notify the central administration in Luxembourg of the orders executed by them which relate to registered securities, in order to ensure (i) that the data relating to investors is updated in the register of unitholders or shareholders and (ii) that the registered certificates or confirmations of investment may be forwarded from Luxembourg to the new investors.

2.3. Duties of the central administration in Luxembourg and of the marketing intermediaries in respect of the prevention of money laundering of drug trafficking proceeds.

Circular IML 89/57 of 15 November 1989 on the money laundering of drug trafficking proceeds is in principle applicable to Luxembourg UCIs.

When considering the particular way in which the UCI industry is operating, notably in the area of marketing, it appears that it is often extremely difficult for the central administration in Luxembourg to know the identity of investors for whom the subscription and redemption orders are collected by Luxembourg or foreign intermediaries.

Considering the above, certain derogations are permitted for subscription and redemption orders collected by intermediaries established, or whose activities in this respect are exercised in a country which belongs to the Financial Action Task Force on Money Laundering (FATF) established after the Summit of the Arch in June 1989 or which applies the recommendations issued by this Task Force.

The central administration in Luxembourg is not obliged to check the identity of investors, whose orders originate from such intermediaries, given that this control is being performed in the country where these orders are collected. The status of the foreign intermediary must however be verified and unusual transactions must be monitored.

In respect of subscriptions or redemption orders collected by intermediaries established in countries which do not apply the recommendations issued by the FATF, the central administration in Luxembourg is fully responsible for compliance with the rules specified in Circular IML 89/57.

3. Maintenance of the register of unitholders

The requirement for the register of unitholders to be kept in Luxembourg not only implies that such registers must be permanently available there, but also that the central administration in Luxembourg must perform the registrations, alterations or deletions necessary to ensure the regular update thereof.

Where the central administration in Luxembourg uses a remote-access computing network as technical support for the performance of these duties, it may, subject to applying the security and protection measures described under heading 1. above and whilst preserving the confidentiality required by legal and regulatory requirements, use the network to access and store in the processing unit the registration of personal data relating to unitholders. The processing unit therefore has the storage facility required for the maintenance of the register of unitholders.

Distributors who are connected to the remote-access computing network used may, through this network, transmit to the central administration in Luxembourg the information relating to the issue and redemption orders collected by them so that it can trigger the necessary procedures in the network to update the data of the unitholders' register stored in the processing unit.

4. Drawing-up of prospectuses, financial reports and other documents intended for investors.

The requirement for prospectuses, financial reports and other documents intended for investors to be drawn up in cooperation with the central administration in Luxembourg only relates to the intellectual tasks necessary for the drawing-up of these documents as opposed to the physical realisation thereof. For the performance of these tasks, this requirement does not exclude limited recourse to experts, advisers and other specialised providers of services established abroad.

Since technical or purely physical tasks are not addressed by this requirement, the central administration in Luxembourg may use the services of printers or other providers of services established abroad in connection with the physical production of the documents intended for investors.

5. Correspondence and dispatch of prospectuses, financial reports and other documents intended for investors.

The requirement for correspondence and dispatch of prospectuses, financial reports and other documents intended for investors to be made from Luxembourg is intended to safeguard the confidentiality of data relating to investors who directly apply to the central administration in Luxembourg to place their subscription orders or whose names appear in the register of unitholders.

Apart from the case specified below, only the central administration in Luxembourg may, in accordance with this objective, carry out from Luxembourg, the dispatches intended for the investors referred to above even where these dispatches concern documents printed abroad. As an exception to this rule, dispatches to the relevant investors may be carried out from abroad (e.g. from the printer's address) provided such dispatches are made under the supervision of the central administration in Luxembourg. It must then ensure by adequate measures of protection that non-authorised third parties may not access data relating to investors for whom the dispatches are intended.

Chapter E. Repealed[1]

[1] Circular CSSF 18/697

Chapter F. Rules applicable to UCITS governed by Part I of the Law of 30 March 1988.

I. Intervals at which the issue and redemption prices must be determined.

UCITS must determine the issue and redemption prices of their units or shares at sufficiently close and fixed intervals, being at least twice a month.

II. Redemption by UCITS of their units or shares.

As already mentioned in heading I. of Chapter C. above, UCITS are required to redeem their units or shares directly or indirectly at the request of investors.

In this connection, one has to recall that UCITS must avoid any restrictions whose object is to submit the exercise of the right to redeem to conditions and procedures which would render redemptions practically impossible or needlessly and arbitrarily complicated and less frequent.

It remains however that a UCITS may, subject to adequate justification of the necessity thereof, provide in its constitutional documents that the management bodies may, in particular circumstances (e.g. in the case of temporary liquidity shortage) or where redemption requests received in connection with the same dealing day exceed a certain proportion of the number of securities outstanding, either provide for a delay of settlement of redemptions during a pre-determined period of time, or for a proportional reduction of all redemption requests so that the threshold level is not exceeded. The latter is only permitted however provided that any proportion of a redemption request which is not honoured by virtue of this possibility, is treated as if the request had been made for the next following dealing day or days until full settlement of all of the original redemption requests.

III. Requirements in respect of the composition of assets.

1. Investment in transferable securities.

Subject to the exceptions provided for in Chapter 5 of the Law of 30 March 1988, the investment of the assets of UCITS must be exclusively made in transferable securities which are either admitted to an official stock exchange listing or traded

on another regulated market which operates regularly and is recognised and open to the public.

It follows that the authorised investments of UCITS must simultaneously meet the following two essential conditions:

- firstly, they must qualify as transferable securities;
- secondly, these transferable securities must be admitted to an official stock exchange listing or traded on another regulated market which operates regularly and is recognised and open to the public.

Neither the Directive 85/611/EEC, nor the Law of 30 March 1988 provide a definition of the concept of "transferable securities".

A problem may therefore arise where in specific cases involving Luxembourg or foreign securities, it is not clear, *prima facie*, whether the securities qualify as transferable securities.

In the case of Luxembourg securities, the IML will continue to rely on the Luxembourg practice which adopted the interpretation according to which the words "transferable securities" mean quoted securities, that is securities which are capable of being quoted irrespective of whether their admission to an official stock exchange listing has effectively taken place or not. According to this precedent, a quotation is deemed possible where the determination of a single price may be envisaged; this is the case where securities do not significantly differ from one another either by their amount, maturity or in any other material respect.

The above criteria are not applied however for the qualification of foreign securities as transferable securities. In this case, it is the IML policy to align itself with the definition of the relevant securities made by the respective regulations of the countries concerned.

The terms "regulated, operating regularly, recognised and open to the public" as used to designate the definition criteria of the markets referred to above are defined neither by the Directive 85/611/EEC nor by the Law of 30 March 1988.

In the absence of such a definition, the IML considers that the following meaning should be given to these terms:

- regulated: the essential characteristic of a regulated market is the clearing which presupposes the existence of a central market organisation for the execution of orders. Such a market can be further distinguished by its multilateral order matching (general matching of bid and offers enabling the establishment of a single price), transparency (maximum distribution of information amongst buyers and sellers giving them the possibility to follow the evolution of the market so that they may ensure that their orders have been carried out at current conditions) and the neutrality of its organiser (the organiser's role must be limited to recording and supervision);
- recognised: the market must be recognised by a state or by a public authority which has been delegated by that state or by another entity which is recognised by that state or by that public authority, such as a professional association;
- operating regularly: securities admitted to this market must be traded at a certain fixed frequency (no sporadic trading);
- open to the public: the securities traded on this market must be accessible to the public.

2. Debt instruments which are treated as equivalent to transferable securities pursuant to Article 40(2)b) of the Law of 30 March 1988.

Securities referred to here are regularly traded money market instruments whose residual maturity exceeds 12 months.

3. Investments in liquid assets.

In addition to the investments authorised pursuant to heading 1. above, a UCITS may hold ancillary liquid assets.

This term not only covers cash and short-term bank deposits, but also regularly traded money market instruments whose residual maturity does not exceed 12 months.

The term "ancillary" means in this context that liquid assets may not in themselves constitute an investment objective, the exclusive object of UCITS being the investment of their assets in transferable securities. The Law of 30 March 1988 therefore does not prohibit a UCITS from holding a significant amount of liquid assets during a certain amount of time due to certain circumstances provided that

such investment in liquid assets does not become the investment objective of the UCITS.

4. Investments in closed-ended UCIs.

The restrictions imposed by Article 44 of the Law of 30 March 1988 on the purchase of units of open-ended UCIs do not apply to the investment in units of closed-ended UCIs.

The units of closed-ended UCIs are indeed considered as being similar to any other transferable security and are therefore, with respect to investment rules, subject to the general rules applicable to transferable securities.

IV. Borrowings.

The restrictions, to which the borrowings of UCITS are subject, do not prohibit a UCITS from acquiring foreign currency by way of a back to back loan. A "back to back" loan refers to the case whereby a UCITS borrows foreign currency in the context of the acquisition and safekeeping of foreign transferable securities and deposits with the lender, its agent or any other person designated by it, an amount in domestic currency equal to or greater than the amount borrowed.

V. Investment limits calculation method as established by Chapter 5 of the Law of 30 March 1988.

The investment limit percentages to be complied with by UCITS must be applied to the net assets of UCITS.

Chapter G. Rules applicable to UCITS subject to Part II of the Law of 30 March 1988.

I. Intervals at which the issue and redemption prices must be determined.

UCITS must determine the issue and redemption prices of their units or shares at sufficiently close and fixed intervals, being at least once a month, subject to the exceptions provided for by the Law of 30 March 1988.

II. Investment limits.

The purpose of the investment limits is to ensure that investments are sufficiently liquid and diversified. It is clear that certain of these limits do not apply to the categories of UCITS defined under heading II.4. of Chapter C. above insofar as they are incompatible with the investment policy defined for each of these categories. Subject to this exception UCITS may not in principle:

a) invest more than 10% of their assets in securities which are not listed on a stock exchange and are not traded on another regulated market which operates regularly and is recognised and open to the public;
b) acquire more than 10% of the same type of securities issued by the same issuing body;
c) invest more than 10% of their net assets in securities issued by the same issuing body.

The aforementioned restrictions are not applicable to securities issued or guaranteed by a Member State of the OECD or their local authorities or public international bodies with community, regional or global scope.

The restrictions mentioned under items a), b) and c) above are applicable to the purchase of units of UCIs of the open-ended type if such UCIs are not subject to risk diversification requirements comparable to those provided for by this circular for UCIs subject to Part II of the Law of 30 March 1988.

It is reminded that units of closed-ended UCIs are treated in the same way as other transferable securities and are therefore subject to the general rules applicable to transferable securities.

The possibility to invest in units of other UCIs must not be used to avoid the provisions of Article 70 of the Law of 30 March 1988.

If it is intended to make investments in other UCIs, the prospectus must expressly state this possibility. Should it be intended to make investments in other UCIs of the same promoter, the prospectus must also specify the nature of the fees and expenses which may arise out of such an investment.

III. Borrowings.

UCITS may borrow the equivalent of up to 25% of their net assets without restriction as to the intended use thereof. This limit does not apply to the category of UCITS defined in heading II.4.3. of Chapter C. above.

IV. Provisions applicable to UCITS which are subject to Chapter 11 of the Law of 30 March 1988.

1. Information to be provided in the constitutional documents.

The constitutional documents must *inter alia* specify
- the principles and methods of valuation of assets;
- the time allowed for payment in respect of issues (and redemptions, if any);
- the conditions which permit suspension of issues (and redemptions, if any).

2. Valuation of assets.

Unless otherwise provided for in the constitutional documents, the valuation of the assets of UCITS referred to herein must be based, in the case of officially listed securities, on the last known stock exchange price, unless such a price is not representative. For securities which are not officially listed and for securities which are listed but for which the latest price is not representative, the valuation shall be based on the probable realisation value which must be estimated with prudence and in good faith.

3. Purchases and sales of securities held in the portfolio.

The purchase and sale of securities held in the portfolio of the UCITS concerned can only be carried out at prices consistent with the valuation criteria specified in heading 2. above ("Valuation of assets").

Chapter H. Rules applicable to all UCITS.

Pursuant to Article 41 of the Law of 30 March 1988 UCITS are authorised

- to employ techniques and instruments relating to transferable securities provided that such techniques and instruments are used for the purpose of efficient portfolio management;
- to employ techniques and instruments intended to provide protection against exchange rate risks in the context of the management of their assets.

The techniques and instruments which UCITS are authorised to use under this provision are more fully described under headings I. and II. of this Chapter. The use of other techniques and instruments is in principle not permitted.

Where a UCITS wishes to use the techniques and instruments described below, this must be expressly mentioned in its prospectus. In such cases, the prospectus must list the types of transactions envisaged and specify the purpose thereof and the conditions and limits within which such transactions may be made. As the case may be, the prospectus must also include a description of the risks inherent in the transactions envisaged.

I. Techniques and instruments relating to transferable securities.

For the purpose of efficient portfolio management, a UCITS may participate in

- transactions relating to options;
- transactions relating to financial futures and options thereon;
- transactions relating to securities lending;
- repurchase agreements.

1. Transactions relating to options on transferable securities.

The purchase and writing of call and put options by a UCITS is permitted provided that such options are traded on a regulated market which is operating regularly, recognised and open to the public.

When entering into these transactions, the UCITS must comply with the following rules:

1.1. Rules applicable to the purchase of options.

The total premiums paid for the acquisition of call and put options outstanding and referred to herein may not, together with the total of the premiums paid for the purchase of call and put options outstanding and referred to in heading 2.3. below, exceed 15% of the net assets of the UCITS.

1.2. Rules to ensure the coverage of the commitments resulting from option transactions.

Upon the conclusion of contracts whereby call options are written, the UCITS must hold either the underlying securities, or equivalent call options or other instruments capable of ensuring adequate coverage of the commitments resulting from such contracts, such as warrants. The underlying securities related to call options written may not be disposed of as long as these options are in existence unless such options are covered by offsetting options or by other instruments that can be used for that purpose. The same restriction applies to equivalent call options or other instruments which the UCITS must hold where it does not have the underlying securities at the time of the writing of such options.

As an exception to this rule, a UCITS may write call options on securities it does not hold when entering into the option contract provided that the following conditions are met:

- the aggregate exercise (strike) price of such uncovered call options written shall not exceed 25% of the net assets of the UCITS;
- the UCITS must at any time be able to ensure the coverage of the position taken as a result of the writing of such options.

Where it writes put options, the UCITS must be covered during the entire duration of the option contract by adequate liquid assets which may be used to pay for the securities which could be delivered to it should the put option be exercised by the counterparty.

1.3. Conditions and limits for the writing of call and put options.

The aggregate of the commitments arising from the writing of put and call options (excluding call options written in respect of which the UCITS has

adequate coverage) and the aggregate of the commitments from the transactions referred to in heading 2.3. hereafter may not, at any time, exceed the value of the net assets of the UCITS.

In this context, the commitment on call and put options written is deemed to be equal to the aggregate of the exercise (striking) prices of those options.

1.4. Rules concerning regular information intended for the public.

In its financial reports, the UCITS must identify the portfolio securities which are the subject of an option and individually indicate every call option written on securities which are not held in the portfolio. It must also break down by category of options the aggregate of the exercise (strike) prices of options outstanding as at the reference date of the relevant reports.

2. Transactions relating to futures and option contracts on financial instruments.

Except for transactions by private agreement mentioned under heading 2.2. below, the transactions described herein may only relate to contracts that are traded on a regulated market which is operating regularly, recognised and open to the public.

Subject to the conditions specified below, these transactions may be made for hedging or other purposes.

2.1. Transactions whose purpose is to hedge risks associated with the evolution of stock markets.

A UCITS may sell stock index futures to provide general protection against the risk of an unfavourable evolution of the stock markets. For the same purpose, it may also write call options on stock indices or purchase put options thereon.

The hedging purpose of these transactions presupposes that there exists a sufficient correlation between the composition of the index used and the corresponding portfolio.

In principle, the aggregate commitments resulting from futures contracts and stock index options may not exceed the aggregate estimated market value of the securities held by the UCITS in the corresponding market.

2.2. Transactions whose purpose is the hedging of interest rate risk.

A UCITS may sell interest rate futures contracts for the purpose of achieving a global hedge against interest rate fluctuations. It may also for the same purpose write call options or purchase put options on interest rates or enter into Over The Counter (OTC) interest rate swap contracts with highly rated financial institutions specialised in this type of operation.

In principle, the aggregate of the commitments relating to futures contracts, options and swap transactions on interest rates may not exceed the aggregate estimated market value of the assets held by the UCITS which are to be hedged, expressed in the currency corresponding to those contracts.

2.3. Transactions whose purpose is other than hedging.

Besides option contracts on transferable securities and contracts on currencies, a UCITS may, for a purpose other than hedging, purchase and sell futures contracts and options on any kind of financial instruments provided that the aggregate commitments in connection with such purchase and sale transactions together with the amount of the commitments relating to the writing of call and put options on transferable securities does not exceed at any time the value of the net assets of the UCITS.

The call options written on transferable securities for which a UCITS has adequate coverage are excluded from the calculation of the aggregate amount of the commitments referred to above.

In this context, the concept of the commitments relating to transactions other than options on transferable securities is defined as follows:

- the commitment arising from futures contracts is deemed equal to the value of the underlying net positions payable on those contracts which relate to identical financial instruments (after netting all purchase and sale positions), without taking into account the respective maturity dates and

- the commitment deriving from options purchased and written is equal to the aggregate of the exercise (strike) prices including the net sales positions of each underlying asset without taking into account the respective maturity dates.

It is reminded that the aggregate amount of premiums paid for the acquisition of call and put options outstanding which are referred to herein, may not, together with the aggregate of the premiums paid for the acquisition of call and put options on transferable securities mentioned in heading 1.1. above, exceed 15% of the net assets of the UCITS.

2.4. Periodical information intended for the public.

In its financial reports, the UCITS must separately indicate for each of the categories of transactions mentioned in headings 2.1., 2.2. and 2.3. above the total amount of commitments deriving from operations outstanding as at the reference date of the relevant reports.

3. Securities lending transactions.

UCITS may enter into securities lending transactions provided the following rules are complied with:

3.1. Rules intended to ensure the correct execution of lending transactions.

A UCITS may only participate in securities lending transactions within a standardised lending system organised by a recognised securities clearing institution or by a highly rated financial institution specialised in this type of transaction.

In relation to its lending transactions, the UCITS must in principle receive collateral, whose value, at the conclusion of the lending agreement, must be at least equal to the overall value of the securities lent.

This collateral must be given in the form of cash and/or of securities issued or guaranteed by Member States of the OECD or by their local authorities or by supranational institutions and organisations with community, regional or

global scope, and blocked in the name of the UCITS until termination of the lending contract.

3.2. Conditions and limits of lending transactions.

Lending transactions may not be carried out on more than 50% of the aggregate market value of the securities in the portfolio. This limit is not applicable where the UCITS has the right, at any time, to terminate the contract and obtain restitution of the securities lent.

Lending transactions may not be extended beyond a period of 30 days.

3.3. Periodical information intended for the public.

The UCITS must indicate in its financial reports the overall valuation of securities lent at the reference date of the relevant reports.

4. Repurchase agreements.

UCITS may enter into a repurchase agreement which consists of the purchase and sale of securities whereby the terms of the agreement entitle the seller to repurchase the securities from the purchaser at a price and at a time agreed to by the two parties at the conclusion of the agreement.

The UCITS may act either as purchaser or seller in repurchase transactions. Its entering into such agreements is however subject to the following rules:

4.1. Rules intended to ensure the correct execution of repurchase agreements.

The UCITS may purchase or sell securities in the context of a repurchase agreement only if its counterparty is a highly rated financial institution specialised in this type of transaction.

4.2. Conditions and limits of repurchase transactions.

During the lifetime of a repurchase agreement, the UCI may not sell the securities which are the object of the agreement either before the repurchase

of the securities by the counterparty has been carried out or the repurchase period has expired.

Where the UCITS is open-ended, it must ensure that the sum of all repurchase agreements is limited such that it is able, at all times, to meet its obligations to redeem its own shares.

4.3. Periodical information intended for the public.

In its financial reports, the UCITS must separately indicate for purchases and sales subject to repurchase obligations, the total amount of repurchase agreements outstanding at the reference date of the relevant reports.

II. Techniques and instruments intended to hedge currency risks to which UCITS are exposed within the context of portfolio management.

In order to protect its assets against currency fluctuations, UCITS may enter into transactions the objects of which are currency forward contracts as well as the writing of call options and the purchase of put options on currencies. The transactions referred to herein may only concern contracts which are traded on a regulated market which is operating regularly, recognised and open to the public.

For the same purpose, the UCITS may also enter into forward sales of currencies or exchange currencies on the basis of Over The Counter (OTC) agreements with highly rated financial institutions specialised in this type of transaction.

The hedging objective of the aforementioned transactions presupposes the existence of a direct relationship between such transactions and the assets to be hedged. This implies that transactions made in one currency may in principle not exceed the valuation of the aggregate assets denominated in that currency nor exceed the period during which such assets are held.

In its financial reports, the UCITS must indicate, for the different types of transactions made, the aggregate amount of commitments relating to transactions outstanding as at the reference date of the relevant reports.

Chapter I. Rules applicable to UCIs other than UCITS.

The Law of 30 March 1988 does not provide for the collective investment objective of UCIs other than UCITS which means that such UCIs may carry out investments in assets other than transferable securities.

The detailed provisions which provide investors in traditional UCITS with certain safety guarantees may not be applied entirely as they stand to UCIs whose objective differs from that of UCITS, in particular with respect to the specific nature of the investment policy of the UCIs, which makes it impossible to apply certain operational rules which must be observed by traditional UCITS. UCIs whose objective differs from the objective of traditional UCITS must therefore be submitted to a certain extent to alternative regimes whose rules are differentiated according to the nature of their investments.

To date, the supervisory authority has set up separate rules for three types of specialised UCIs the principal object of which is either:

- the investment in venture capital which refers to the investment in securities of unlisted companies either because these companies have been recently established or because they are still in the course of development and therefore have not yet obtained the stage of maturity required to have access to stock markets; or
- the investment in commodity futures contracts and/or financial futures contracts and/or in options; or
- the investment in real estate.

The separate rules established by the supervisory authority for each of the three specialised types of UCIs do not replace the general rules which remain applicable, rather they only modify certain rules in order to adapt them to the particularities of each type of UCI.

The particular rules applicable to the UCIs referred to here are specified under headings I., II. and III. hereafter.

In specific cases, the IML may grant certain derogations from these rules on the basis of adequate justification.

I. Rules of the particular regime applicable to UCIs whose principal objective is investment in venture capital.

The rules provided for hereafter modify the rules of the general regime with respect to the following points:

1. Management and supervisory bodies.

With regard to the professional qualification, the directors of the management bodies and, where applicable, the investment advisers, must possess a specific experience in the field of investment in venture capital.

2. Investment restrictions.

The investment restrictions applicable to traditional UCITS do not apply to UCIs referred to in this section with the exception that the investment in venture capital must be diversified to such an extent that an adequate spread of the investment risk is ensured. In order to ensure a minimum spread of such risks, the UCIs concerned may not invest more than 20% of their net assets in any one company.

3. Issue and redemption of units or shares.

The date of determination of the issue and redemption prices will depend upon the frequency of the periods of issue and redemption of units or shares.
Where the investors have the right to redeem their units or shares, the UCI may impose certain restrictions on such a right. These restrictions must be clearly described in the prospectus.

4. Special requirements.

Apart from these general rules which are derived from those applicable to traditional UCITS, those UCIs whose principal object is the investment in venture capital must also comply with the following special requirements:

4.1. Type of securities.

The total of bearer and registered shares issued by the UCI must represent a number of shares or units whose value at the time of issue is at least equal to 500,000 francs.

4.2. Remuneration of investment management and advisory bodies.

If the remuneration of the investment management and advisory bodies is higher than that usually received by similar bodies from traditional UCITS, the prospectus must state whether the additional remuneration is also payable on assets which are not invested in venture capital.

4.3. Information for investors.

The annual and semi-annual reports of the UCI must contain information on the development of the companies in which it has invested. In the event of a sale of securities held in the portfolio, the UCI must publish separately for each investment the amount of profit or loss. In addition, the financial statements must mention where there is a potential conflict of interest between the interests of a director of the investment management or advisory bodies and the interests of the UCI.

4.4. Specific information to be disclosed in the prospectus.

The prospectus must contain a detailed description of the investment risks inherent in the investment policy of the UCI and of the nature of the conflicts of interest which could arise between the interests of a director of the investment management and advisory bodies and the interests of the UCI.

Furthermore, the prospectus must include a statement indicating that since an investment in such a UCI represents an above average risk, the UCI in question is only suitable for those persons who are able to assume such risks and that it is advisable for the average subscriber to invest therein only a part of the sum intended for long-term investment.

II. <u>Rules of the particular regime applicable to UCIs whose principal objective is investment in futures contracts (commodity futures and/or financial futures) and/or in options.</u>

The rules provided for hereafter modify the rules of the general regime with respect to the following points:

1. Management and supervisory bodies.

With regard to the professional qualification, the directors of the management bodies and, where applicable, the investment advisers must possess a specific experience in the field of investment in commodities, financial futures and options respectively.

2. Investment restrictions.

2.1. Margin deposits relating to commitments on long or short futures contracts, and call and put options written may not exceed 70% of the net assets of the UCI, the balance of 30% representing a liquidity reserve.

2.2. The UCI may only enter into futures contracts traded on an organised market. Futures contracts underlying options must also comply with this condition.

2.3. The UCI may not enter into commodity contracts other than commodity futures contracts. By way of derogation, the UCI may, with cash settlement, acquire precious metals which are negotiable on an organised market.

2.4. The UCI may only acquire call and put options which are traded on an organised market. Premiums paid for the acquisition of options outstanding are included in the 70% limit provided for under heading 2.1. above.

2.5. The UCI must ensure an adequate spread of investment risks by sufficient diversification.

2.6. The UCI may not hold an open forward position in any one futures contract for which the margin requirement represents 5% or more of net assets. This rule also applies to open positions resulting from options written.

2.7. Premiums paid to acquire options outstanding which have identical characteristics may not exceed 5% of net assets.

2.8. The UCI may not hold an open position in futures contracts concerning a single commodity or a single category of financial futures for which the margin required represents 20% or more of net assets. This rule also applies to open positions resulting from options written.

3. Borrowings.

The UCI may only borrow up to the equivalent of 10% of its net assets provided such borrowings may not be used for investment purposes.

4. Special requirements.

Apart from these general rules which are derived from those applicable to traditional UCITS, those UCIs whose principal object is the investment in futures contracts and/or options must also comply with the following special requirements:

4.1. Type of securities.

The total of bearer and registered shares issued by the UCI must represent a number of shares or units whose value is at least equal to 500,000 francs at the time of issue.

4.2. Remuneration of managers and investment advisers.

If the remuneration of the investment management and advisory bodies is higher than that usually received by similar bodies from traditional UCITS, the prospectus must state whether the additional remuneration is also payable on assets which are not invested in futures contracts and/or options.

4.3. Information for investors.

The annual and semi-annual reports of the UCI must contain information on the amount of profit or loss realised by the UCI, for each category of futures and option contracts that has been carried out. In addition, the financial statements must quantify the commissions paid to brokers and the fees paid to the investment management and advisory bodies.

4.4. Specific information to be disclosed in the prospectus.

The prospectus must contain a detailed description of the trading strategy followed by the UCI with respect to futures contracts and options as well as the investment risks inherent in the investment policy. In particular, mention must be made that the futures and options markets are extremely volatile and that the risk of loss is very high.

In addition, the prospectus must include a statement indicating that the UCI in question is only suitable for persons who are able to assume such risks since the investment in that UCI represents an above average risk.

III. Rules of the particular regime applicable to UCIs whose principal objective is investment in real estate.

By real estate assets this circular refers to:

- property consisting of land and/or buildings registered in the name of the UCI;
- share holdings in real estate companies (including debt securities of such companies) whose exclusive object and purpose is the acquisition, promotion and sale as well as the letting and agricultural lease of property, provided that these share holdings must be at least as liquid as the property rights held directly by the UCI;
- property related long-term interests such as surface ownership, lease-holds and option rights on real estate assets.

The rules provided for hereafter modify the rules of the general regime with respect to the following points:

1. Management bodies.

With regard to the professional qualification, the directors of the management bodies and, where applicable, the investment advisers, must possess a specific experience in real estate assets.

2. Investment restrictions.

The investment restrictions applicable to traditional UCITS do not apply to UCIs referred to in this section. Nevertheless, the investment in real estate assets must be diversified to such an extent that an adequate spread of the investment risk is ensured. In order to achieve a minimum spread of such risks, the UCIs concerned may not invest more than 20% of their net assets in a single property, such a restriction being effective at the date of acquisition of the relevant property. Property whose economic viability is linked to another property is not considered a separate item of property for the purpose of this restriction.

This 20% rule does not apply during a start-up period which may not extend beyond four years after the closing date of the initial subscription period.

3. Issue and redemption of securities.

The net asset value on which the issue and redemption prices of the securities are based must be determined at least once a year, namely at the end of the financial year, as well as on each day on which shares or units are issued or redeemed. In respect of real estate assets, management may use the valuation established at the year end throughout the following year unless there is a change in the general economic situation or in the condition of the properties which requires new valuations to be carried out under the same methods as those used for the annual valuation.

Where the investors have the right to redeem their units or shares, the UCI may impose certain restrictions thereon. In addition, where it is justified, notably with regard to a specific investment policy, the UCI has the obligation to restrict such a right of redemption. These restrictions must be clearly described in the prospectus. The UCI may in particular provide for deferred settlements for cases when it does not hold sufficient liquid assets to immediately honour the redemption requests received.

4. Special requirements.

Apart from these general rules which are derived from those applicable to traditional UCITS, UCIs whose principal object is the investment in real estate must also comply with the following special requirements:

4.1. Remuneration of investment management and advisory bodies.

If the remuneration of the investment management and advisory bodies is higher than that usually received by similar bodies from traditional UCITS, the prospectus must indicate whether such additional remuneration is also payable on assets which are not directly or indirectly invested in real estate assets.

4.2. Valuation of properties.

Management must appoint one or more independent property valuers with a specific experience in the field of property valuation.

At the end of the financial year, management must instruct the property valuer(s) to examine the valuation of all properties owned by the UCI or by its affiliated real estate companies.

In addition, properties may not be acquired or sold unless they have been valued by the property valuer(s), although a new valuation is unnecessary if

the sale of the property takes place within six months after the last valuation thereof.

Acquisition prices may not be noticeably higher, nor sales prices noticeably lower, than the relevant valuation except in exceptional circumstances which are duly justified. In such cases, the managers must justify their decision in the next financial report.

4.3. Borrowings.

The aggregate of all borrowings of the UCI may not exceed on average 50% of the valuation of all its properties.

4.4. Financial statements.

The audit of the accounts of the UCI and of real estate companies which are more than 50% funded by the UCI either by way of equity or loans, must be carried out under the responsibility of one and the same *réviseur d'entreprises* (statutory auditor). The accounts of these entities must in principle be drawn up as per the same date.

At the end of each half year, the accounts of the UCI must be consolidated with those of the real estate companies referred to in the preceding paragraph subject to the relevant legal requirements.

Where the UCI holds minority interests in real estate companies whose securities are not listed on a stock exchange nor traded on another regulated market operating regularly, recognised and open to the public, the UCI must provide either for a partial consolidation at year end or for a valuation on the basis of the probable sale value estimated with prudence and in good faith by its management. For the valuation of minority shareholdings held in real estate companies whose securities are listed on a stock exchange or traded on another regulated market operating regularly, recognised and open to the public, the stock exchange or market value must be taken into consideration.

In its annual and semi-annual reports, the UCI must clearly explain the accounting principles applied for the consolidation of its own accounts with those of affiliated real estate companies.

The inventory of properties included in the annual and semi-annual reports must, for each category of property held by the UCI or its real estate companies, indicate the overall purchase or cost price, the insured value and the market value.

In the financial statements, properties must be shown at market value.

4.5. Specific information to be disclosed in the prospectus.

The prospectus must give a description of the investment risks inherent in the UCI's investment policy. In addition, the prospectus must provide details of the nature of the commissions, expenses and charges to be borne by the UCI and the methods used for their calculation and allocation.

Chapter J. Rules applicable to UCIs with multiple compartments.

I. General principle.

The Law of 30 March 1988 introduced into Luxembourg law the concept of UCIs with multiple compartments, commonly referred to as "umbrella funds".

These are UCIs set up as common funds or investment companies with several compartments within a single entity. These compartments are used for instance to invest in transferable securities denominated in different currencies or of different geographic regions or economic sectors. From a practical point of view, it proved to be useful to offer investors the possibility within a single entity to choose between several currencies or assets. Furthermore, after having invested in one compartment, the investor may easily switch to one or several other compartments. The conversion from one compartment to the other within the same UCI in principle does not incur the higher rates of commission associated with the case whereby the investor invests in legally separate and independent undertakings.

The Law of 30 March 1988 provides that a multiple compartment UCI constitutes a single legal entity. This implies that a multiple compartment UCI, where certain compartments would normally fall under Part I of the Law of 30 March 1988 whilst other compartments would fall under Part II, is to be considered to fall in its entirety under Part II because of the criterion of the "single legal entity".

Nevertheless, the Law of 30 March 1988 provides that the constitutional documents of multiple compartment UCIs may provide that in respect of the relations between unitholders, each compartment will be treated as a separate entity.

Considering that the multiple compartment UCI, existing as a single legal entity, consists of different compartments and that the investor may restrict his investment to one or the other compartment, it appears inevitable that the units or shares of this single legal entity can have different values. For this reason, the Law of 30 March 1988 provides in its Article 111 that the units and shares may be of different values with or without mention of value, depending on the legal form which has been chosen. This is a derogation clause relating to Article 37 of the Law of 10 August 1915 on commercial companies (as amended) which, in particular, provides that the capital of limited liability companies is divided into shares of equal value.

The experience obtained of multiple compartment UCIs has lead to the drawing-up of the rules set out under headings II., III. and IV. hereafter.

II. Common funds.

In order to remain within the scope of Article 111(2) of the Law of 30 March 1988 which provides that multiple compartment UCIs constitute a single legal entity, the following conditions must be met:

- the different compartments of the fund must have a common generic denomination and a single management company which determines the investment policies and their application to the relevant compartments through a single board of directors of the management company;
- the custody of the assets of the different compartments of the fund must be ensured by a single depositary who may however use, to the same extent as those funds with a single portfolio, correspondents in different geographic regions;
- the fund must be governed by a single set of management regulations which form its legal basis. Subject to derogations which may be granted by the IML on the basis of adequate justification, the management regulations must notably determine for each compartment the same redemption conditions for each category of units and the same general valuation, suspension, redemption and investment restriction principles;
- the supervision of the fund must be carried out by a single *réviseur d'entreprises* (statutory auditor);
- the unitholders shall in principle, subject to reasonable limits, be able to switch from one compartment to the other without payment of commissions;
- the management regulations must indicate the currency in which the combined position of the fund is expressed and which is obtained by aggregating the financial positions of all the compartments in the fund.

In addition to the preceding more specific conditions, common funds with multiple compartments must also comply with the following conditions:

- the certificates or other documents evidencing the rights of unitholders may only differ with regard to the designation of the respective compartments for which they are issued;
- the issue and redemption of units attributable to each compartment must be carried out at a price arrived at by dividing the net asset value of the corresponding compartment by the number of outstanding units in that compartment;

- the investment and borrowing restrictions provided for by the Law of 30 March 1988 or by this circular must be complied with inside each compartment with the exception of those restricting the holding of securities of a single issuer which shall also apply to the aggregate of all of the different compartments.

As regards more particularly the condition of minimum net assets resulting from Article 22 of the Law of 30 March 1988, it is considered that this condition is complied with if a common fund with multiple compartments reaches minimum assets of 50 million francs in respect of the aggregate of all its compartments within a period of 6 months following its authorisation.

As a consequence of the above, the provisions of the first paragraph of Article 23 of the Law of 30 March 1988 only become applicable after the aggregate net assets of all the compartments of a multiple compartment common fund taken together have fallen below two thirds of the legal minimum of 50 million francs.

III. Investment companies.

The specific characteristics associated with the concept of multiple compartment investment companies call for the following observations:

1. In a multiple compartment investment company the net asset value of a share is calculated on the basis of the net assets of the compartment in respect of which the share is issued. The value of shares of the same company shall therefore necessarily differ from one compartment to the other.

   However, this difference in share value representing the share capital of a multiple compartment investment company has no impact on the voting rights attached to such shares. Indeed, each share gives the right to one vote within the context of the exercise of voting rights and all shares participate equally in the decisions to be taken in general meetings.

   For the sake of clarity, it is recommended that this equal treatment of shareholders in respect of the exercise of their voting rights is emphasised in the articles of incorporation of a multiple compartment investment company.

   Furthermore, the articles should in addition distinguish between the decisions affecting all shareholders and which are to be considered in a single general meeting and the decisions only affecting the specific rights of shareholders of one compartment and which are therefore taken by the general meeting of one compartment.

2. Every company must have a share capital represented by shares.

The Law implies that there be

- a single share capital;
- denominated in a single currency;
- the nominal or accounting par value being expressed in that same currency;
- the annual accounts also being expressed in that same currency.

It follows from there that the share capital of a multiple compartment investment company must be denominated in a single reference currency. However, the net asset value of each compartment is denominated in the currency of the relevant compartment.

In the interests of a clear understanding of the operating mechanism of multiple compartment investment companies, it is recommended that the articles of these companies clearly indicate the preceding particularities.

3. The articles of a multiple compartment investment company, similarly to the articles of investment companies with a single portfolio, must indicate the circumstances of suspension of the calculation of the net asset value of the company and consequently the suspension of issues and redemptions of shares of that company.

The articles of a multiple compartment investment company must furthermore provide for the circumstances of suspension of the calculation of the net asset value (and consequently of issues and redemptions) of the individual compartments.

4. The investment and borrowing restrictions provided for by the Law of 30 March 1988 or by this circular must be complied with inside each compartment with the exception of those restricting the holding of securities of a single issuer which shall also apply to the aggregate of the different compartments.

IV. Common rules applicable to all UCIs with multiple compartments.

It must be clearly stated in the constitutional documents of multiple compartment UCIs irrespective of whether they are established in the form of common funds or in the form of investment companies, that for the purposes of the relations between

unit- or shareholders, each compartment shall be treated as a single entity with its own funding, capital gains and losses, expenses etc...

The launch of a new compartment is subject to the authorisation of the IML and the update of the prospectus, where necessary, by means of an insert.

Chapter K. Contents of the file which must accompany the application for authorisation of UCIs.

In support of their application for entry on the list provided for by Article 72(1) of the Law of 30 March 1988, Luxembourg UCIs must submit to the IML an application file which, *inter alia*, contains the following:

a) Drafts of

- the constitutional documents (articles of incorporation of the management company and management regulations or articles of incorporation of the UCI),
- the prospectus and all other information and/or marketing material intended for investors,
- any agreements such as depositary and advisory agreements;

b) Indication of the name of the depositary in Luxembourg with a precise and detailed description of the human and technical resources at its disposal for the accomplishment of all the tasks related to its duties;

c) Indication of the name of the *réviseur d'entreprises* (statutory auditor);

d) Information on the organisation of the central administration of the UCI in Luxembourg with a precise and detailed description of the human and technical resources at its disposal for the accomplishment of all the tasks linked to its duties;

e) Information on the promoter(s) such as recent financial reports;

f) Biographical notices of administrators and managers;

g) Information on the method used to market the securities issued by the UCI, the countries of distribution and the targeted investors.

Where the information and documents mentioned in the preceding items b), d), e) and f) have already been submitted to the IML in respect of a previous application they must not be resubmitted provided that no change has occurred in the interim.

Chapter L. Information and marketing material intended for investors.

I. Prospectus.

1. Contents of the prospectus.

The prospectus must include the information necessary for investors to be able to make an informed judgment on the investment proposed to them.

It shall contain the information provided for in Schedule A annexed to the Law of 30 March 1988 insofar as such information does not already appear in the documents annexed to the prospectus in accordance with Article 87(1) of the same Law. In addition, it must carry a statement that no person is authorised to give any information other than that contained in the prospectus or in the documents referred to therein and which may be consulted by the public.

The IML may require the publication of all additional information it deems necessary in order to provide objective and complete information to the public.

Every prospectus must be dated and may be used only as long as the information contained therein remains accurate. The essential elements of the prospectus must be kept up to date. This could be achieved by inclusion in the periodical financial reports.

UCIs may in principle only enter into the transactions specifically mentioned in their prospectus. This particularly applies to the transactions concerned by Chapter H. above. Reference is made to the detailed provisions of that Chapter.

2. Specific rules applicable to multiple compartment UCIs.

In the interests of providing correct information to investors, it is recommended that the rules set out under headings II. to IV. of Chapter J. above should be stated clearly not only in the constitutional documents of multiple compartment UCIs, but also in the prospectuses of such UCIs.

Multiple compartment UCIs must provide for a single prospectus covering all of their compartments. In this prospectus, it must be specified that commitments

in relation to a single compartment bind the whole of the UCI unless contrary arrangements have been agreed with the relevant creditors.

Besides this prospectus, multiple compartment UCIs may provide for the publication of separate prospectuses for each of their compartments. Where this facility is used, it is mandatory that the following information, clearly indicated, be included in the separate prospectuses:

- Indication that the compartment concerned, to which the separate prospectus relates, does not constitute a separate legal entity, rather that there exists other compartments which together with the compartment in question form a single entity;
- Indication that for the purposes of the relationship between unit- or shareholders, each compartment is considered a separate entity with its own funding, capital gains and losses, expenses etc.;
- Indication that commitments in respect of the compartment to which the separate prospectus relates, bind the whole UCI unless contrary arrangements have been agreed to with the relevant creditors;
- Indication that there exists a prospectus which includes a complete description of all the compartments of the UCI with an indication as to where that prospectus may be obtained.

3. Visa.

In order to ensure the correct identification of the prospectuses which have obtained the "*nihil obstat*" of the IML, such prospectuses are visa stamped by the IML and returned complete with visa to the person who submitted the file.

For this purpose, the IML must receive five copies of each prospectus when final with respect to both content and presentation. The visa stamp may in no circumstances be used for publicity purposes.

II. Repealed[*]

[*] Circular CSSF 05/177.

III. Financial reports.

1. Periodicity and content of financial reports.

Every UCI must publish an annual report for each financial year and a semi-annual report covering the first six months of the financial year.

The financial year ends in principle on the last calendar day of a month.

The annual and semi-annual reports must be published within the following time limits with effect from the end of the period to which they relate:
- four months in the case of the annual report;
- two months in the case of the semi-annual report.

In respect of the content of the financial reports, reference is made to Article 86(2), (3) and (4) of the Law of 30 March 1988 as well as to Schedule B annexed to that Law. In the same context, it is reminded that the financial reports must include the information required by the provisions of Chapter H. above in respect of the transactions referred to in that Chapter.

The *réviseur d'entreprises'* (statutory auditor's) report provided for by Article 89(1) of the Law of 30 March 1988 must be included in the annual reports.

2. Specific rules applicable to multiple compartment UCIs.

Multiple compartment UCIs must include in their financial reports separate information on each of their compartments as well as aggregate information on all of their compartments. The information referred to hereby is provided for by Article 86(2), (3) and (4) of the Law of 30 March 1988 as well as in Schedule B annexed to that Law, provided that headings II., III., IV., VI. and VII. of that Schedule are not to be considered for the compilation of aggregate information.

The separate financial reports, which must be established for each of the compartments, must be expressed in their respective reference currency. For the purpose of the establishment of the aggregate situation of the UCI, these financial reports must be added together following conversion into the denomination of the share capital, where the UCI has been formed as an

investment company, or into the currency determined for that purpose by the management company, where the UCI has been formed as a common fund.

Alongside the full report to be established pursuant to these rules, multiple compartment UCIs may provide for the publication of separate financial reports for each of their compartments. Where this facility is used, the conditions to be respected for the publication of separate prospectuses are applicable by analogy to this case. Reference is made in this connection to heading I.2. above.

Where a separate annual report is established for each compartment of a multiple compartment UCI, the *réviseur d'entreprises'* (statutory auditor's) report provided for by Article 89(1) of the Law of 30 March 1988 must also be included in the relevant report unless the *réviseur d'entreprises* (statutory auditor) establishes separate reports for each compartment. If separate *réviseur d'entreprises'* (statutory auditor's) reports are established, they may be published in the separate annual reports of the relevant compartments in lieu of the report covering all the compartments which make up the UCI.

3. Publication of the financial reports and communication thereof to the IML.

The UCI must transmit to the IML two copies of its annual and semi-annual reports when final with respect to both contents and presentation, no later than at the moment of publication. It is not necessary to submit drafts to the IML prior to publication.

Financial reports are not subject to the visa formality.

Where periodical reports contain errors or omissions, the IML reserves the right to determine if an amended report must be published.

IV. <u>Use of the prospectus and periodical reports.</u>

Pursuant to the provisions of Article 91(1) of the Law of 30 March 1988 the prospectus and the latest annual report as well as the subsequent semi-annual report, if published, must be offered to subscribers free of charge before the conclusion of a subscription contract.

In this respect, the question arises whether, before the conclusion of a subscription contract, the above-mentioned documents must be provided to the subscriber upon his request only or whether they must be provided in any event even in the absence of such a request.

On this matter, the IML considers that the subscription contract may be entered into without the subscriber being aware of or, even received, a copy of the prospectus and periodical reports, provided these documents had been offered to him in the conditions provided for.

It follows from the above that Article 91(1) of the Law of 30 March 1988 does not prohibit that the subscription form is attached not to the prospectus, but to a brief information brochure which indicates how subscribers may obtain the prospectus and the periodical reports.

It is clear that for the purposes of distributing their securities abroad, Luxembourg UCIs must comply with the legal, regulatory and administrative provisions which govern the use of the prospectus and periodical reports in the respective distribution countries.

Chapter M. Financial information intended for the IML.

In accordance with Article 94(1) of the Law of 30 March 1988, the UCIs must transmit to the IML the financial information set out in the table (IML: "Monthly financial information of UCIs") a template of which is annexed to this circular, on a monthly basis.

I. Reference date.

In principle, the last day of every month shall be the reference date for the preparation of financial information to be transmitted to the IML.

However, the preceding rule is not compulsory for UCIs which calculate their net asset value at least once a week. For this category of UCIs, the reference date may be the last day on which the net asset value of that month is calculated.

This derogation is also valid for the UCIs which calculate the net asset value per unit or per share at least monthly if the day of this calculation falls either in the last week of the reference month or in the first week of the following month. The financial information to be transmitted to the IML must then be prepared on the basis of the data available at the calculation date nearest to the last day of the month.

UCIs which do not calculate their net asset value per unit or per share on a monthly basis need only indicate in their monthly statements the amounts effectively booked in the accounts at the end of the month excluding any non-accounting estimates.

II. Reporting deadlines

UCIs must report the monthly information to the IML within a period of 20 days after the reference date.

III. Reporting currency and portfolio.

The table for the transmission of monthly financial information must indicate the reporting currency used for the preparation of the information set out in point I.1., I.2. and III. of the table concerned. This reporting currency must be the currency used to calculate the net asset value per unit or share of a UCI.

The term "portfolio" within the meaning of point II. of the same table means all the investments which constitute the object of the investment policy of a UCI.

IV. Change in the net asset value per unit or per share.

Where the net asset value per unit or per share varies over 10% compared to the value calculated at the end of the preceding month, explanations must be given as to the reasons for this variation.

V. UCIs with multiple compartments.

The monthly financial statements must be drawn up for each compartment separately by using the reporting currency of the compartment concerned and a global situation must be drawn up in the currency used for the overall financial statements of the UCI.

Chapter N. Rules applicable to management companies of common funds.

I. Information obligation of management companies *vis-à-vis* the IML.

Immediately following the approval thereof by the general meeting of shareholders, the management companies of common funds must transmit to the IML their annual accounts together with the directors' report and the report of the external auditors responsible for the audit of the annual accounts.

II. Authorisation of the shareholders of a management company.

Pursuant to Article 71(3) of the Law of 30 March 1988 the managers of a management company must be of sufficiently good repute and have the requisite experience for the performance of their duties.

To that end, the names of the managers of the management company, and of every person succeeding them in office, must be communicated forthwith to the supervisory authority.

The Law of 30 March 1988 defines managers as being the persons who represent the management company or who effectively determine the strategy thereof.

This raises the question as to whether the shareholders of the management company are to be considered as managers for whom authorisation by the supervisory authority is required. This question must be answered in the affirmative insofar as one has to consider that the shareholders effectively determine the strategy of the management company.

The principal shareholders of the management company of a common fund must therefore be of sufficient repute and have the requisite experience for the performance of their duties and must, in this respect, obtain the authorisation of the IML.

Chapter O. Distribution rules applicable in Luxembourg.

The marketing rules with which UCIs must comply in Luxembourg when their units or shares are distributed therein derive in particular from:

- the law of 25 August 1983 on the legal protection of consumers;
- the law of 27 November 1986 regulating certain commercial practices and penalising unfair competition; and
- the law of 16 July 1987 on door-to-door sales, itinerant trade, display of goods and canvassing for orders.

Chapter P. Obligation of UCIs to inform the IML of the audit performed by the *réviseur d'entreprises* (statutory auditor).

UCIs must forthwith communicate to the IML without being specifically requested to do so, the declarations, reports and written observations made by the *réviseur d'entreprises* (statutory auditor) within the scope of the controls which he must carry out pursuant to Article 89 of the Law of 30 March 1988. The documents to be communicated must *inter alia* include the written observations issued by the *réviseur* (auditor) which generally take the form of a management letter addressed to the UCI.

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Yours faithfully,

INSTITUT MONETAIRE LUXEMBOURGEOIS

Jean GUILL	Jean-Nicolas SCHAUS	Pierre JAANS
Director	Director	Director General